

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petitions	:	
of	:	
JING FONG RESTAURANT, INC.,	:	DETERMINATION
SHUI LING LAM AND CHUNG TSUI	:	DTA NOS. 820355, 820356,
	:	820357 AND 830358
for Revision of Determinations or for Refund of	:	
Sales and Use Taxes under Articles 28 and 29 of	:	
the Tax Law for the Period June 1, 2000 through	:	
May 31, 2003.	:	

Petitioners, Jing Fong Restaurant, Inc., 20 Elizabeth Street, New York, New York 10013, Shui Ling Lam, 5415 8th Avenue, Brooklyn, New York 11220, and Chung Tsui, 265 Cherry Street, Apartment # 18C, New York, New York 10002, filed petitions for revision of determinations or for refunds of sales and use taxes under Articles 28 and 29 of the Tax Law for the period June 1, 2000 through May 31, 2003.

A hearing was held before Thomas C. Sacca, Administrative Law Judge, at the offices of the Division of Tax Appeals, 641 Lexington Avenue, New York, New York, on October 27, 2005 at 10:30 A.M., with all briefs to be submitted by February 10, 2006, which date began the six-month period for the issuance of this determination. Petitioner appeared by Louis Miu, CPA. The Division of Taxation appeared by Christopher C. O'Brien, Esq. (Jennifer A. Murphy, Esq., of counsel).

ISSUES

I. Whether a portion of the banquet service charge stated on the invoice to be paid to the service employees is subject to the imposition of sales tax.

II. Whether petitioners have established any basis warranting reduction or elimination of penalties imposed.

FINDINGS OF FACT

1. On July 14 and 23, 2003, the Division of Taxation (“Division”) sent a letter to petitioner Jing Fong Restaurant, Inc., advising that its New York State sales and use tax records for the period June 1, 2000 through May 31, 2003 had been scheduled for audit. An attachment to the letter requested that the following records for the audit period be made available: sales tax returns, Federal income tax returns, New York State corporation tax returns, general ledgers, general journals, sales invoices, fixed asset purchases, expense purchase invoices, bank statements, cash receipts journal and cash disbursements journal. The letter further noted that the concentration of the audit would be the examination of tips per guest checks. On April 19, 2004, an appointment letter and attached list of records requested was sent to petitioners’ representative, Mr. Louis Miu.

2. Petitioner Jing Fong Restaurant, Inc., operated a Chinese restaurant in the Chinatown district of Manhattan. The restaurant also contained a large room which was used for private banquet parties. Shui Ling Lam and Chung Tsui were corporate officers of petitioner.

3. On each check relating to a banquet held in the restaurant, the following statement was placed:

SERVICE CHARGE

A service charge of 15% is added to all food & beverage charges. A minimum of 77% of the 15% service charge will be distributed to the banquet servers, bus-boy, waiter, captain, bartender & hostess. The remaining portion of the service charge is retained by the restaurant in connection with management, supervisory, sales, catering, kitchen personnel and other costs relating to the function.

Between June 2000 and September 2000, the split of the service charge was 23% to the restaurant and 77% to the employees. Beginning in October 2000, and through the end of the audit period, the split of the service charge was 21% to the restaurant and 79% to the employees. The service charge statement on the banquet invoices for the period beginning in October 2000 reflected the percentage allocation change.

4. During the periods June 2000 through September 2000 and October 2000 through May 2003, the corporation reported the 23% portion and 21% portion, respectively, of the service charge as income, and paid the applicable sales tax thereon.

5. Following his review of petitioner's books and records, the auditor was unable to reconcile the full service charge figure with any book entry. He was unable to determine if the 77% portion (later 79% portion) of the service charge was actually given to the employees, and he therefore determined that the balance of the service charge constituted unreported taxable receipts. Sales tax due on these unreported taxable receipts was \$122,744.85. Penalties for the reporting of the incorrect amount of tax due and the underreporting of less than 75% of the correct amount of sales tax due were assessed. The auditor also determined that the corporation had properly reported the management portion of the service charge as taxable income in its books and records.

6. On December 29, 2003, the Division of Taxation issued to the corporation a Notice of Determination assessing additional sales tax due for the period June 1, 2000 through November 30, 2000 in the amount of \$18,905.23, plus penalty and interest. On April 2, 2004, the Division issued to the corporation a second Notice of Determination assessing additional sales tax due for the period December 1, 2000 through May 31, 2003 in the amount of \$103,839.62, plus penalty and interest. In addition, on April 29, 2004, the Division issued notices of determination to Shui

Ling Lam and Chung Tsui, as officers of Jing Fong Restaurant, Inc., assessing additional sales tax due for the period June 1, 2001 through May 31, 2003 in the amount of \$83, 233.12, plus penalty and interest.

7. Following a banquet and the presentation of the banquet check to the customer, the service charge was collected by a manager of the corporation. The employees' portion was immediately given to the lead service employee who in turn distributed the money to the remainder of the banquet service staff. The percentage that each service employee received was determined by the service that particular individual performed during the banquet, according to a structured formula which was established by the employees. Thus, according to the policy and practice of petitioner, all the money collected as part of the service charge which was designated for payment to the service employees was distributed to them pursuant to a pre-established formula.

8. In 1998, the New York State Attorney General's Office reviewed the practice and policy of Jing Fong Restaurant, Inc., with regard to the handling of the service charge and found the corporation in compliance with the requirements of Labor Law § 196-d. The Attorney General's Office found that the employees were, in fact, receiving their portion of the service charge.

CONCLUSIONS OF LAW

A. Tax Law § 1105(d)(i) imposes sales tax upon "receipts . . . from every sale of food and drink of any nature . . . including in the amount of such receipts any cover, minimum . . . or other charge made to patrons or customers" Tax Law § 1101(b)(3) defines receipts as "[t]he amount of the sale price of any property and the charge for any service taxable under this

article . . . without any deduction for expenses” The service charge billed to customers is taxable, as a receipt from the sale of food or drink, unless: “(1) the charge is separately stated on the bill or invoice given to the customer; (2) the charge is specifically designated as a gratuity; and (3) all such monies received are paid over in total to employees.” (20 NYCRR 527.8[1].)

B. Petitioner has established that the employee portion of the service charge as designated on the banquet receipt was in fact turned over to the employees following each banquet. Submitted into evidence were affidavits of waiters employed by petitioner and an affidavit of an attorney who provided labor and employment advice to petitioner. In addition, testimony was offered which supported petitioner’s position that following each banquet, the employee portion of the service charge was divided among the employees according to the function they performed at the banquet.

C. Labor Law § 196-d provides, in relevant part, as follows:

No employer or his agent or an officer or agent of any corporation, or any other person shall demand or accept, directly or indirectly, any part of the gratuities, received by an employee, or retain any part of a gratuity or of any charge purported to be a gratuity for an employee. . . . Nothing in this subdivision shall be construed as affecting the allowances from the minimum wage for gratuities in the amount determined in accordance with the provisions of article nineteen of this chapter nor as affecting practices in connection with banquets and other special functions where a fixed percentage of the patron’s bill is added for gratuities which are distributed to employees, nor to the sharing of tips by a waiter with a busboy or similar employee.

A banquet service charge (in whole or in part) becomes the property of the service employee or the employer depending on how the service charge is characterized to the patron and how the monies are treated by the employee and the employer. The common practice in the industry of dividing the banquet service charge between the service employees and the employer complies

with section 196-d of the Labor Law, provided that adequate notice is given to the patrons as to how the service charge will be divided.

D. The sales and use tax regulations dealing with the taxability of gratuity or service charges are meant to insure that if there is an additional charge, such charge is to be considered a gratuity and, as such, will be paid over to the service employees. The regulations require that for a gratuity or service charge to be exempt from the imposition of sales tax, the charge must be separately stated on the customer invoice, specifically designated as a gratuity and all such monies received must be paid over to the employees (20 NYCRR 527.8[l]). The restaurant's treatment of the service charge clearly meets the requirements of the regulation. The banquet invoice provides in a clear and unequivocal written statement that there will be a separate service charge. Although not specifically called a "gratuity," the statement on the banquet invoice makes clear that the service charge is a "tip" or "gratuity" by indicating that the charge will be distributed to the "banquet servers, busboy, waiter, captain, bartender and hostess." Finally, as previously noted, all the monies earmarked for the employees as indicated on the banquet invoice go directly to the service employees. Although it could be argued that the third requirement of the regulation is not met because some of the service charge is paid over to petitioner, the purpose of the regulation is met by the language of the service charge statement which clearly indicates to the patrons of the banquet what portion of the service charge is going to management and what portion is going to the employees. In addition, as previously discussed, all the monies intended for the employees as indicated by the banquet service charge statement are actually paid to the service employees. Therefore, pursuant to 20 NYCRR 527.8(l), the portion of the banquet service charge that is paid to the employees is not subject to the imposition of sales tax.

E. The petitions of Jing Fong Restaurant, Inc., Shui Ling Lam and Chung Tsui are granted, and the notices of determination issued on December 29, 2003, April 2, 2004 and April 29, 2004 are cancelled. In light of Conclusion of Law “D”, Issue II is rendered moot.

DATED: Troy, New York
July 13, 2006

/s/ Thomas C. Sacca
ADMINISTRATIVE LAW JUDGE